MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2020/2021

BAC4674 – INTEGRATED CASE STUDY IN ACCOUNTING

(All Sections/Groups)

17 MARCH 2021
9.00 a.m. – 12.00 p.m.
(3 Hours)

INSTRUCTIONS TO STUDENT

1. This question paper consists of **FOUR** pages (excluding cover page) with **THREE** questions only.

2. Answer **ALL** questions. All questions carry equal marks and the distribution of the marks for each question is given.

3. Write your answers and workings in the Answer Booklet provided.

Merkat Mall

Merkat Mall (Merkat) is a major supermarket chain with a loyal customer base and a 30% share of the Malaysian supermarket sector.

Merkat Mate

Merkat is proposing to take advantage of the recent COVID-19 Movement Control Order and popularity of mobile apps for food delivery by launching its own mobile app, under the name of Merkat Mate. This will reduce the pressure felt by Merkat's traditional, mature retail business as a result of restricted movement, and will take advantage of rising demand for delivery services. Merkat Mate will operate from 30 branches within the largest existing Merkat stores and will also provide online payment facilities. The strategy is to offer Merkat customers contactless shopping and the marketing literature will emphasise "convenience and customisation through close but contactless relationships".

Initially Merkat Mate will offer simple online grocery shopping experience. Merkat has studied other competitors who have launched similar apps and found that their apps were not fully successful as the supporting logistics and customer service was not up to expectations, leading to dissatisfied customers. Customers of other grocery shopping apps found that the items offered were limited and delivery services are often fully booked. Considering its market size, Merkat intends to invest heavily into the backend infrastructure and hire new staff to be able to meet the expected demand.

Once Merkat Mate have all been launched successfully, it will offer e-wallet and credit card services for customers. Unlike other competitors which have moved into selected personal finance products via joint ventures with major local banks, Merkat is planning to control its own banking operations. It will hire its own financial services specialists to run its branches and staff its customer service call centre. In view of the current digital trend, the Malaysian government is keen to increase digital financial services providers and Merkat has already been granted a banking licence.

Customer loyalty card scheme and integrated information system

Merkat has over10 million customers in Malaysia and manages its relationship with them via a customer loyalty card. The loyalty card allows customers to earn points in return for cash spent in Merkat stores. Points can be converted into vouchers that can be used to reduce the cost of future purchases. The loyalty card forms part of an integrated data analytics and knowledge management information system which allows Merkat to track the shopping habits of its customers.

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The other key element of the integrated system is a sophisticated electronic point of sale (EPOS) and inventory control system. As soon as a sales transaction is recorded, this system updates inventory records, provides valuable sales information regarding product demand and profitability, and facilitates automated purchasing from suppliers. This has enabled Merkat to reduce costs by increasing the frequency and accuracy of ordering, leading to lower levels of inventory and wastage.

The data collected from the various elements of the integrated system are logged in a centralised database with an advanced search engine. The data analytics feature of the system allows Merkat to build a profile of each customer with a loyalty card. This profile can then be used for a variety of purposes including pricing, decisions as to which product ranges to stock, research, marketing and customer service. One of the key benefits is improved customer segmentation, enabling Merkat to promote low price or high-quality items as appropriate. The information is also sold to a number of the company's suppliers which use it to refine and develop their products.

Whilst most other supermarkets operate similar customer loyalty schemes, none is as far-reaching as Merkat's, which was the first of its kind. Merkat's research suggests that one in four Malaysia adults belongs to its customer loyalty scheme. A key advantage for Merkat is that the scheme enables it to identify other products that the customer is likely to be interested in, based on their profile and spending patterns. Merkat plans for the loyalty card scheme to be a key driver of competitive advantage for its expansion into credit services, especially, as none of the existing financial providers operates a loyalty card scheme. It will provide an immediate customer list for direct marketing purposes and the data may help to assess a customer's credit-worthiness. Merkat intends to offer its customers a Merkat Mall credit card to stand alongside the standard loyalty card scheme. This will further enhance its database by giving it access to information about non-Merkat purchases made by its customers.

Merkat criticised

The following is an extract from an article that appeared recently in a national newspaper: "Supermarket giant Merkat has been criticised recently. Its customer loyalty card scheme has been labelled as a sophisticated spy system by some critics, allowing it to exploit customers by capturing information that they are not in a position to withhold and then using it to sell them things they don't need. As well, there is a risk that this private shopping information could fall into the wrong hands and might one day be used against people.

Merkat has also been accused of further tightening supplier payment terms to improve its own cash flow, despite continuing to make huge profits – indeed this may be where the money for its proposed expansion into banking services is coming from. Suppliers are, of course, prevented from complaining about low margins and onerous terms and conditions because of fears that they will lose Merkat's business."

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Financing Merkat Mate

Developing Merkat Mate requires high investments into the information technology infrastructure as well as creating a customer service and logistics department to package and deliver the online orders.

- Debt:equity ratio (by market values) of Merkat unchanged after the diversification.
- An appropriate equity beta for a company that operates climbing walls is 1.90 at a debt:equity ratio (by market values) of 4:6.
- If the Merkat Mate project goes ahead, the overall equity beta of Merkat will be made up of 80% existing operations and 20% Merkat Mate.

The following information relates to Merkat without the Merkat Mate project. Extracts from the most recent financial statements are as below:

Statement of Financial Position
30 November 2019

	RM (million)
Ordinary share capital (RM0.20 shares)	365
Retained earnings	4,788
	5,153
5% Redeemable debentures at nominal value	2,200
	7,353

On 30 November 2019, Merkat's ordinary shares each had a market value of RM3.60 (cum-div) and an equity beta of 1.10. For the year ended 30 November 2019, the dividend declared was RM0.10 per ordinary share and the earnings yield (earnings per share divided by ex-div share price) was 7%.

Merkat's debentures had a market value at 30 November 2019 of RM99 (cum-interest) per RM100 nominal value and are redeemable at par on 30 November 2023.

The market return is expected to be 7% per annum and the risk free rate 2% per annum. Assume that the corporation tax rate will be 17% per annum for the foreseeable future.

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REQUIRED:

QUESTION ONE

(a) Using the Capital Asset Pricing Model, calculate a Weighted Average Cost of Capital that is suitable for appraising the Merkat Mate project and explain the rationale for using this as the discount rate for the project.

(15 marks)

(b) By calculating an overall equity beta and using the CAPM, estimate the overall WACC of Merkat assuming that the Merkat Mate project goes ahead and comment upon the implications for the value of Merkat of any change from the WACC that you have calculated in (a) above.

(10 marks)
(Total: 25 marks)

QUESTION TWO

In preparation for a meeting of Merkat's senior executives, the operations director has asked you to prepare a report which:

(a) Explains the FIVE (5) potential benefits of an effective data analytics and information system for Merkat.

(15 marks)

(b) Discuss how Merkat has used its information systems to create competitive advantage in the supermarket industry.

(15 marks)

(c) Assesses the suitability, feasibility and acceptability of Merkat's proposed expansion into the e-wallet and credit card sector.

(30 marks)

(Total: 60 marks)

QUESTION THREE

Discuss the ethical issues raised by the newspaper article in respect of Merkat's customer loyalty card and its treatment of suppliers.

(15 marks)

[TOTAL: 100 MARKS]

End of Paper.